

**IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
TWENTIETH JUDICIAL DISTRICT, DAVIDSON COUNTY, PART IV**

COLONIAL PIPELINE COMPANY,)
)
 Plaintiff,)
)
 vs.)
)
 JUSTIN P. WILSON, Tennessee Comptroller)
 of the Treasury; TENNESSEE STATE)
 BOARD OF EQUALIZATION; and)
 THE MEMBERS OF THE TENNESSEE)
 STATE BOARD OF EQUALIZATION, et al.,)
)
 Defendants.)

CASE NO. 05-478-IV

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J.C. & M.

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MEMORANDUM AND FINAL ORDER

Plaintiff, Colonial Pipeline Company ("Plaintiff," "Colonial Pipeline," or "Colonial"), brings this facial constitutional challenge against statutes that allow Tennessee to tax Plaintiff's property as public utility property and to tax its pipelines and surface equipment as real property. The defendants in this suit are: 1) Defendant, Justin P. Wilson, Comptroller of the Treasury, State of Tennessee, who, as Comptroller, is head of Tennessee's Office of State Assessed Properties and is a member of the State Board of Equalization; 2) Defendant, Tennessee Board of Equalization; 3) Defendant, Governor Bill Haslam, who is also a Member and Chairman of the Tennessee State Board of Equalization; 4) Defendant, Dwight E. Tarwater, as Counsel to the Governor, and a member of the Tennessee State Board of Equalization; 5) Defendant, Tre Hargett, is Secretary of State of the State of Tennessee and a member of the Tennessee State Board of Equalization; 6) Defendant, David H. Lillard, Jr., is the State Treasurer of the State of Tennessee and a member of the Tennessee State Board of Equalization; 7) Defendant, Richard H. Roberts, is the Commissioner of Revenue of the State of Tennessee and a

member of the Tennessee State Board of Equalization; 8) Defendant, Bill Bennett, a member and Vice-Chair of the Tennessee State Board of Equalization; and 9) Defendant, Betty Burchett, a member of the Tennessee State Board of Equalization (collectively referred to as "the State"). See Tenn. R. Civ. P. 25.04. The individual defendants were sued in their official capacities. Plaintiff is claiming that the statutes classifying its property as public utility property and its pipelines as real property each violate the equal protection clauses of the state and federal constitutions, the Uniformity Clause of Tennessee Constitution, and the Commerce and Supremacy Clauses of the United States Constitution.¹

In 1973, the General Assembly enacted legislation which had the effect of classifying Colonial Pipeline as a public utility and its property as public utility property. This classification, which was codified as Tenn. Code Ann. § 67-5-501(8), provided that public utility property includes all property used or held for use in the operation of a public utility. It lists gas, electric, and several other kinds of companies as public utilities, including pipeline companies. In 2004, the Tennessee General Assembly adopted HB 3289 which, *inter alia*, specifically classified pipelines as real property. See 2004 Tenn. Pub. Acts. 719. Later codified as Tenn. Code Ann. § 67-5-501(9)(B)(iii), the new law classified as real property "[m]ains, pipes, pipelines and tanks permitted or authorized to be built, laid or placed in, upon, or under any public or private street or place for conducting steam, heat, water, oil, electricity or any property, substance or product capable of transportation or conveyance therein or that is protected thereby." *Id.*

¹ Plaintiff's Supremacy Clause assertions are not separate challenges, but are included within Colonial's Commerce Clause challenge that reclassification of its pipeline as real property discriminates against interstate commerce and that the classification of its property as public utility property results in an undue burden on interstate commerce. See First Amended and Restated Complaint for Injunctive and Declaratory Relief, ¶¶ 65, 111.

Tenn. Code Ann. § 67-5-501(9)(B)(iii), which classified pipelines as real property, and Tenn. Code Ann. § 67-5-501(8), which classifies the property of pipeline companies as public utility property, are the statutes being challenged here.

In Tennessee, local government assesses most commercial and residential property. Certain subcategorized properties, such as public utility property, are assessed by a centralized state agency, the Office of State Assessed Properties ("OSAP"). OSAP assesses Colonial's properties. *See Colonial Pipeline Co. v. Morgan*, 263 S.W.3d 827, 833 (Tenn. 2008). Article III, § 28 of the Tennessee Constitution was amended effective January 1, 1973, to classify property for tax assessment purposes, requiring equality and uniformity in each class or subclass throughout Tennessee. As a result of the amendment and other developments since 1973, "industrial and commercial" personal property is assessed at 30% of its value; "industrial and commercial" real property is now assessed at 40% of its value; and "public utility" personal and real property is assessed at 55% of its value. *See id.*

The *ad valorem* tax rates applicable to a particular taxpayer are commonly referred to by stating the real property rate first and the personal property next. So, if a company's real estate rate is 40% and its personal property rate is 30% for *ad valorem* tax purposes, that company's tax rate will be referred to as 40/30. Colonial's public utility status and the reclassification of its pipelines as real property put Colonial at a 55/55 *ad valorem* tax status. Colonial is claiming that its rates should be no higher than 40/30 under the industrial and commercial classification which applies to many companies Colonial contends are competitors and/or other similarly situated centrally assessed taxpayers.

Essentially, these classifications impact Colonial Pipeline's *ad valorem* tax in two related ways. Colonial is claiming that none of its property, real or personal, should be taxed as public utility property (taxed at 55% of value), but asserts, for example, that its real property should be taxed as industrial and commercial property (taxed at 40% of value). Secondly, Colonial is claiming that its pipelines should be taxed as industrial and commercial tangible personal property (taxed at 30% of value) as opposed to public utility real property (taxed at 55% of value). See *Colonial Pipeline Company v. Morgan*, 263 S.W.3d 827, 833 (Tenn. 2008). If Colonial's pipelines were taxed as public utility tangible personal property, it would be potentially subject to be taxed at 55% of its value, except that Colonial would be entitled to a 15% equalization reduction. Consequently, both classifications (real property and public utility) operate together to subject Colonial's real and personal property to the highest 55/55 tax bracket.

In March 2006, the Court granted dismissal in favor of Defendants ("the State"), holding that Colonial Pipeline had not exhausted its administrative remedies. The Court of Appeals reversed and the Tennessee Supreme Court affirmed this reversal, remanding the case back to this Court for a resolution of Colonial Pipeline's facial constitutional challenges.² See *Colonial Pipeline v. Morgan*, 263 S.W.3d 827 (Tenn. 2008). In proceedings in this Court, after the Tennessee Supreme Court remanded this case in 2009, the parties disputed what the scope of Colonial's facial challenge should be here. The Court held a two-day trial on certain issues that were arguably best considered in an

² The Tennessee Supreme Court's ruling allowed the Court to decide Plaintiff's facial constitutional challenges while the administrative proceeding was held in abeyance. If the Court rules that the statutes are facially constitutional and that holding is upheld on appeal, then the agency will interpret and apply the challenged statutes and decide any as-applied constitutional challenges the agency is required to reach in order to decide the case.

as-applied proceeding, in the interest of making sure that the appellate courts would have a complete record if this case is appealed.

After remand, on August 27, 2008, Plaintiff filed its First Amended and Restated Complaint for Injunctive and Declaratory Relief (“Amended Complaint”) against Justin P. Wilson, Comptroller of the Treasury, the Tennessee Board of Equalization, and each member of the Tennessee Board of Equalization in their individual capacities. Plaintiff’s Amended Complaint seeks relief declaring unconstitutional the classification of Plaintiff’s pipelines as “real property” under Tenn. Code Ann. § 67-5-501(9) and as “public utility property” under Tenn. Code Ann. § 67-5-501(8) for purposes of *ad valorem* taxation as violative of state and federal Equal Protection Clauses, Tennessee’s Uniform Taxation Clause, the Commerce Clause, and the Supremacy Clause.³ After allowing discovery, the Court held a two-day bench trial on January 9-10, 2012.

Facts

Colonial operates pipelines that transport refined petroleum products (i.e., gasoline, home heating oil, jet fuel, diesel fuel) from Pasadena, Texas (south of Houston) to Linden, New Jersey on the New Jersey side of the New York Harbor. Plaintiff does not transport crude oil, natural gas, liquid petroleum such as propane or butane, or renewable fuels such as ethanol or bio-diesel fuels. Renewable fuels can cause corrosion in Colonial’s pipes and are not otherwise compatible with the products that flow through Colonial’s pipelines.

³ Plaintiff’s Original Complaint for Injunctive and Other Relief (“Original Complaint”), filed on February 22, 2005, challenged its real and personal property *ad valorem* taxation rates, but did not necessarily directly and specifically challenge its classification as a public utility. The challenge to its personal and real property *ad valorem* tax rates, however, implicated Colonial’s classification as a public utility. The Original Complaint brought state and federal equal protection challenges and challenges under the Commerce and Supremacy Clauses; it did not make a claim under Tennessee’s Uniform Taxation Clause.

Colonial's Scheduling and Shipping Support Leader, Mr. Jim Ed "Buster" Brown, Jr., ("Mr. Brown"), described Colonial's business in functional terms as essentially "an underground truck." Transcript ("T"), p. 17.⁴ Its pipelines consist of approximately 5500 miles of pipe traversing the District of Columbia and thirteen states, including portions of Tennessee. Given that Colonial's pipelines are composed of forty-foot sections of pipe that have been welded together, Colonial is able to regularly relocate and replace its pipes located in Tennessee and elsewhere. As part of the process Colonial uses in removing or replacing any of its pipes, it endeavors to restore the owner's land to its original condition. In Tennessee, Colonial has pumping stations, "stubs," or delivery points in Chattanooga, Knoxville, and Nashville. Colonial does not deliver products to any Tennessee location west of Nashville or east of Knoxville.

Colonial Pipeline is a common carrier regulated by the Federal Energy Regulatory Commission ("FERC") and is required to be fair and equitable to its customers. Plaintiff is a transportation company; it does not own, produce, refine, market, purchase, or sell any of the refined petroleum products it transports through its pipelines. In transporting products, Colonial Pipeline basically transports two categories of products: 1) refined petroleum products; and 2) petroleum distillates. Pipeline transportation is slow, reliable, continuous, and safe. Colonial's name is based on its original footprint of serving most of the thirteen original colonies.

Colonial's transportation rates are not volatile; they are not tied to product prices, the impact of natural disasters, or supply distribution issues. It takes ten to fifteen days, at a rate of three or four miles an hour, for product leaving Pasadena, Texas to arrive in the New York Harbor. Similarly, it takes five to ten days for product to reach Nashville,

⁴ The trial transcript consists of two volumes. Because the pages are consecutively numbered, the Court will identify the relevant point in the two-volume transcript by page number.

Tennessee from Pasadena, Texas. Colonial Pipeline transports product in five-day cycles. In other words, Colonial sequences its transportation services in such a way that refiners can count on injecting their product into Colonial's system every five days and receiving terminals can count on Colonial delivering product in five day intervals. In United States markets, refined petroleum products are also transported by barges, railroad, and over-the-road trucks.

FERC sets the rates, via tariffs, that Colonial Pipeline can charge customers for its transportation services. Colonial Pipeline is subject to a grandfathered rate from 1992-1993, adjusted by the Producer Price Index and, perhaps, related factors. Plaintiff does not generally own, in fee simple, the real estate where its pipelines run. Colonial typically secures permission from land owners through license and right-of-way agreements which are memorialized by instruments recorded in public offices where deeds are recorded.

In Tennessee, Colonial is vested with the power of eminent domain. Colonial has used its direct right of eminent domain in Tennessee relatively sparingly, in the sense of filing lawsuits against landowners to obtain right-of-ways.⁵ No other company can use or lease Plaintiff's pipelines, which continuously transport refined petroleum products to Colonial's customers. In addition to some degree of indirect competition in the transport of refined petroleum products via barges, railroad and over-the-road trucks, Colonial's pipelines run roughly parallel to and compete directly with the refined petroleum pipelines of Plantation Pipe Line Company ("Plantation"), over much of Colonial's

⁵ Obviously, Colonial's eminent domain power helped it negotiate right-of-way settlements with landowners in instances when Colonial did not file an eminent domain suit.

routes. Colonial's pipelines were established in the early 1950s. Plantation's pipelines were established in the early 1940s.⁶

In the telephone industry, for example, the incumbent carriers own the cables that could arguably serve as barriers to competition, but they are required to offer for lease cable capability to the non-incumbent carriers at rates designed to allow new entrants into the market without the necessity of building new cable-related infrastructure. In the pipeline industry where Colonial, by analogy, is an incumbent, there are, for logical, structural reasons, no such requirements and, accordingly, any natural barrier which may exist to new entrants entering the market to directly compete against Colonial in the market of transporting petroleum products arguably remain. The parties agree that Colonial is not a true monopoly, even though Colonial arguably has some features of a natural monopoly. Here, fixed or startup costs (relating to infrastructure) in the petroleum pipeline industry are so high that entry of a company into this particular industry would be exceedingly difficult.

In response to federal cases holding that Tennessee's equalization system as it existed after the 1973 amendment to the Tennessee Constitution did not resolve the problem of unequal assessments, the Tennessee General Assembly in 1980 authorized the Tennessee Board of Equalization ("the Board") to adjust public utility property values to achieve equalization with industrial and commercial property. Still, equalization concerns persisted. After a Tennessee appellate ruling declared Colonial's pipelines to be personal property in 2002, the Tennessee legislature amended relevant statutes in 2004 to expressly classify "pipelines" as real property. This amendment prompted this lawsuit, resulting in the Tennessee Supreme Court's decision declaring that Colonial's facial

⁶ While Colonial serves Knoxville, Chattanooga, and Nashville, Plantation serves only Knoxville and Chattanooga.

constitutional challenges could be decided by this Court without the need for it to first exhaust administrative remedies.

Prior to 2004, Tennessee appellate courts determined that Colonial's pipelines were personal property for *ad valorem* tax purposes, which were taxable at a lower rate (40%) than real property (55%). As mentioned earlier, the Tennessee General Assembly amended Tenn. Code Ann. § 67-5-501 in 2004 to modify the definition of real property to include "[m]ains, pipes, pipelines and tanks." *Id.* The effect of this amendment was that Colonial's pipelines would be subject to the higher (55%) real property assessment. Colonial sued in this Court seeking injunctive and declaratory relief. The State moved to dismiss asserting that Colonial had failed to exhaust administrative remedies. This Court granted the motion to dismiss; this dismissal was reversed by the Court of Appeals and the Tennessee Supreme Court. On remand, Colonial's challenge tests the constitutional limits of the State's inherent, plenary power to pass and amend tax statutes in this particular context.

Basic Legal Framework

In summary terms, Plaintiff is making a facial challenge to the Tennessee tax statutes which classify its pipelines as public utility property and real property. Plaintiff is claiming that these statutes violate the equal protection clause, Tennessee's Uniformity Clause, the Commerce Clause and the Supremacy Clause. The Tennessee Supreme Court has carefully identified the stakes involved in a facial constitutional challenge to a statute:

A facial challenge to a statute is the most difficult challenge to mount successfully. The presumption of a statute's constitutionality applies with even greater force when a facial challenge is made. Accordingly, the challenger must establish that no set of circumstances exists under which the statute would be valid. Stated another way, the challenger must demonstrate that the law cannot be constitutionally applied to anyone.

Courts considering a facial challenge to a statute should proceed with caution and restraint because holding a statute facially unconstitutional may result in unnecessary interference with legitimate governmental functions. Accordingly, the courts view facial invalidity as “manifestly strong medicine” and invoke it sparingly and only as a last resort.

There are at least three reasons for the courts’ reticence to invalidate statutes on their face. First, claims of facial invalidity often rest on speculation and thus run the risk of the “premature interpretation of statutes on the basis of factually barebones records.” Second, facial challenges “run contrary to the fundamental principle of judicial restraint” by inviting the courts to “formulate a rule of constitutional law broader than is required by the precise facts to which it is to be applied.” Third, “facial challenges threaten to short circuit the democratic process by preventing laws embodying the will of the people from being implemented in a manner consistent with the Constitution.”

Thus, a successful facial constitutional challenge results in the wholesale invalidation of the statute. While passing on the validity of a statute wholesale may be efficient in the abstract, any gain is often offset by losing the lessons taught by the particular. For this reason, many courts view “as applied” challenges as the “basic building blocks” of constitutional adjudication. “As applied” challenges are preferred because, if they are successful, they do not render the entire statute completely inoperative. In some circumstances, the courts can best fulfill the legislature’s intent by prohibiting only the unconstitutional applications of a statute, while allowing the State to enforce the statute in other circumstances.

Waters v. Farr, 291 S.W.3d 873, 921-23 (Tenn. 2009).

The Tennessee General Assembly has broad taxing authority that courts should not interfere with unless a taxing measure violates the federal or state constitution. *See Sears, Roebuck & Co. v. Woods*, 708 S.W.2d 379, 383 (Tenn. 1986); *Evans v. McCabe*, 52 S.W.2d 159, 160 (Tenn. 1932). Similarly, Tennessee courts “do not decide constitutional questions unless resolution is absolutely necessary to determining the issues in the case and adjudicating the rights of the parties.” *State v. Taylor*, 70 S.W.3d 717, 720 (Tenn. 2002)(citing *Owens v. State*, 908 S.W.2d 923, 926 (Tenn. 1995)).

Tennessee statutes are presumed to be constitutional.⁷ See *Waters v. Farr*, 291 S.W.3d 873, 882 (Tenn. 2009); *Gallaher v. Elam*, 104 S.W.3d 455, 459 (Tenn. 2003). The challenger, as a general proposition, must persuade the court that no set of circumstances exists under which the statute, as written, would be valid. See *U.S. v. Salerno*, 481 U.S. 739, 745 (1987); *Lynch v. City of Jellico*, 205 S.W.3d 384, 390 (Tenn. 2006) (quoting *Davis-Kidd Booksellers, Inc. v. McWherter*, 856 S.W.2d 520, 525 (Tenn. 1993)). States, moreover, may not make or enforce laws that deny any person the equal protection of the laws.

Equal Protection

Colonial's primary facial challenge to the two property tax classifications at issue (public utility property and real property) is on equal protection grounds. It is well-settled that the right to equal protection "is guaranteed by both the United States and Tennessee Constitution." *State v. Tester*, 879 S.W.2d 823, 827 (Tenn. 1994). The equal protection guarantee can be described, in generic terms, as follows:

The constitutional guarantee under the 14th Amendment that the government must treat a person or class of persons the same as it treats other persons or classes in like circumstances. In today's constitutional jurisprudence, equal protection means that legislation that discriminates must have a rational basis for doing so. And if the legislation affects a fundamental right (such as the right to vote) or involves a suspect classification (such as race), it is unconstitutional unless it can withstand strict scrutiny.

Black's Law Dictionary 557 (7th ed. 1999). In broad sweep, Colonial asserts, by pointing out that its pipelines are personal property under Tennessee legal principles that would apply in the absence of the 2004 reclassification statute, that there was no reasonable

⁷ Similarly, the United States Supreme Court has declared that statutes "adjusting the burdens and benefits of economic life come to the Court with a presumption of constitutionality[.]" *Usery v. Turner Elkhorn Mining Co.*, 428 U.S. 1, 15 (1976). The presumption of constitutionality applies to Plaintiff's equal protection and other challenges to the property tax classifications.

basis for the Tennessee General Assembly to reclassify pipelines from personal property to real property for *ad valorem* tax purposes and that this reclassification deprived Colonial of its federal and state right to equal protection and its personal property tax uniformity and equalization rights. Similarly, Colonial claims that there is no reasonable basis for the State to continue to classify Colonial's property as public utility property when Colonial is admittedly not a monopoly and when companies Colonial characterizes as its similarly-situated competitors are treated as non-utility "commercial and industrial" companies taxed at a lower rate. The State counters, urging that although Colonial Pipeline is not a monopoly, it has eminent domain and market power; that many of the competitors identified by Colonial are not similarly situated; that several of Plaintiff's facial constitutional challenges are actually "as applied" constitutional challenges which cannot be considered by this Court now under the Tennessee Supreme Court's ruling; and that a rational basis exists for both tax classifications (real property and public utility property) challenged by Colonial.

Section 1 of the Fourteenth Amendment to the United States Constitution prohibits states, among other things, from making or enforcing any law that denies "any person within its jurisdiction the equal protection of the laws." *Id.* Similarly, Article XI,

Section 8 of the Tennessee Constitution provides, in part, as follows:

The Legislature shall have no power to suspend any general law for the benefit of any particular individual, nor to pass any law for the benefit of individuals inconsistent with the general laws of the land; nor to pass any law granting to any individual or individuals, rights, privileges, [immunities] or exemptions other than such as may be, by the same law extended to any member of the community, who may be able to bring himself within the provisions of such law.

Id. This provision of our state Constitution affords "essentially the same protection" as the United States Constitution's equal protection clause. *State v. Tester*, 879 S.W.2d 823,

827 (Tenn. 1994) (quoting *Tennessee Small Sch. Sys. v. McWherter*, 851 S.W.2d 139, 152 (Tenn. 1993)). Given that no suspect class or fundamental right is implicated by the property tax classifications being challenged here, the rational basis test applies to Plaintiffs' equal protection claims under the federal and state constitutions. See *Tester*, 879 S.W.2d at 828.

The rational basis test is the least rigorous of the tests that courts use to evaluate due process and equal protection claims. Generally speaking, the rational basis test examines whether the challenged legislative classification bears a reasonable relationship to a legitimate state interest. See *Tennessee Small Sch. Sys.*, 851 S.W.2d at 153. "Under this standard, if some reasonable basis can be found for the classification, or if any state of facts may reasonably be conceived to justify it, the classification will be upheld." *Id.* at 153 (quoting *Harrison v. Schrader*, 569 S.W.2d 822, 825 (Tenn. 1978)). In other words, a legislative classification can withstand an equal protection challenge under the rational basis test if a reasonable basis for the classification is articulated and this articulated basis bears some logical relationship to a legitimate state interest, even if this articulated rationale is not itself demonstrated in the evidentiary or legislative record as the actual reason for the classification. This approach defers to the legislature's prerogative to make distinctions and classifications in setting public policy.

Real Property Classification

The "[m]ains, pipes, pipelines and tanks" redefined as "real" property in Chapter 719 certainly include any form of transportation pipeline, such as the oil pipelines and other surface equipment owned and operated by Colonial in Tennessee. Tenn. Code Ann. § 67-5-501(9)(B)(iii). But Chapter 719 does not include any statutory exception for "[m]ains, pipes, pipelines and tanks" used in manufacturing processes, at least so long as

they are used “for conducting steam, heat, water, oil, electricity or any property, substance or product capable of transportation or conveyance therein.” *Id.*

Defendants admit “the State Board has not updated any of its manuals related to the assessment or classification of property to include any information on the effects of Chapter 719 or on how to apply Chapter 719.” Ex. 58; Defendants’ Response to Colonial’s Request for Admission No. 164; *see also* T, p. 409. Likewise, since “the enactment of Chapter 719, the Division of Property Assessments did not update any of its assessment manuals, which local Assessors use as a guide in classifying and assessing real and personal property” of “locally assessed taxpayers.” *Id.*, No. 167. In particular, the “State Board has not removed ‘Tanks’ and ‘Pipelines’ from the Personal Property Tax Schedule provided” for use by local tax assessors “for valuing property for *ad valorem* taxation.” *Id.*, No. 152a.

Based on their guidelines and forms, Defendants acknowledge that “locally assessed pipelines may be assessed as personal rather than real property.” Defendants’ Pre-Trial Brief, at pp. 26-27; *see* T, pp. 407-13. For example, Defendants admit that, in accordance with their instructions to county tax assessors at a recent workshop, the county assessors “consistently” classify locally assessed piping used in manufacturing, as well as piping running from petroleum storage tanks, as “personal” property. T, pp. 408-09 & Ex. 75. Defendants further admit that locally assessed “above ground” tanks, mains, pipes and pipelines continue to be classified as “personal” property per the Defendants’ standard practices. Ex. 58; Defendants’ Responses to Colonial’s First Request for Admission No. 141, 663-778; *see also* T, pp. 411-13 & Ex. 59. Likewise, several local assessors independently confirmed and testified that, relying on Defendants’ guidelines and approved forms, they continue to classify as “Personal” property for *ad*

valorem tax purposes (i) “above ground” storage tanks, (ii) “above ground” pipes or pipelines connected to and supplying petroleum or comparable products to those tanks; and (iii) certain “below ground” pipes or pipeline. Ex. 55: James Gattis Deposition, from p. 8, line 9 to p. 9, line 10; *id.*, p. 11, lines 15-21; *id.*, p. 12, lines 8-15; *see* Ex. 56: Eric Beaupre Deposition, from p. 14, line 7 to p. 24, line 24; *see also* T, pp. 230-31, 407-13 & Ex 59.

As a result, Defendants assert that even though OSAP now classifies central assessed *interstate* pipelines, pipe and tanks as “real” property at the highest 55% “public utility” rate (without the 15% equalization reduction applicable only to “personal” property of “public utility” taxpayers), many county tax assessors relying on the Defendants’ guidelines and forms continue to classify locally assessed *intrastate* pipelines, pipes and tanks as “personal” property at the lowest 30% rate (as opposed to the higher 40% rate applicable to “real” property of “commercial and industrial” taxpayers). *See id.* Colonial’s blue-colored pipes (as well as its transmix tanks and other surface equipment) are being assessed at 55% of their value, while the white-colored pipes (and even larger petroleum storage tanks) of local distributors are generally being assessed at 30% of their value, even though the same refined petroleum is being transported through the same pipe. *See id.*; *see also* T, pp. 245-46 & Ex. 24. From Colonial’s vantage point, the only physical difference between these pipes is the “very expensive” blue color used by Colonial. T, p. 246.

The facial equal protection challenge presented to the Court regarding the reclassification of Colonial’s pipeline as real property is not whether the Tennessee General Assembly can enact a statute specifically designed to supersede a Tennessee appellate court ruling; it is clear that the legislature has this prerogative. The equal

protection question presented to the Court does not necessarily turn on how long-standing or how well-settled the prior classification as personal property may have been in Tennessee jurisprudence. The facial equal protection challenge before the Court is an inquiry into the somewhat related, but different question of whether the new challenged tax classification itself bears a reasonable relationship to a legitimate state interest.

In an equal protection case, the first thing to determine is whether the classes of persons (or companies) being compared are similarly situated. If they are not similarly situated, there is no predicate for an equal protection violation. See *City of Memphis v. Hargett*, 414 S.W.3d 88, 110 (Tenn. 2013). Here, Colonial is largely comparing itself to companies involved in the transportation of refined petroleum products through other conveyances (trucks, barges, and rail) and, to a lesser extent, with a refinery in Memphis that uses pipes to start the distribution process. Defendants urge that these industries are not similarly situated for equal protection purposes. The Court agrees.

Although Colonial, barges, trucks, and rail cars all transport refined petroleum products as part of the distribution chain, they are not similarly situated. Colonial's pipes are buried in the ground in right-of-ways and they extend 5500 miles. Although these pipes were construed as personal property under Tennessee law prior to the statutory change in 2004, it appears clear that reclassifying these pipelines as real property does not create a legitimate question about whether trucks, barges, and rail should be similarly classified. Similarly, the short term piping leading from the Valero refinery in Memphis has a sufficient nexus with the refinery's roles as a manufacturing facility that the Court concludes that these pipes are not similarly situated with Colonial's long term pipeline system which traverses thirteen states and the District of Columbia. Consequently the relatively short piping from the Valero refinery and similar businesses are not similarly

situated with Colonial's pipeline system. There can be no facial equal protection violation, therefore, with respect to the General Assembly's reclassification of pipelines from personal property to real property.

Similarly, and in the alternative, the State has a rational basis for attempting to maximize tax revenue by reclassifying personal property which is closely associated with real property as real property. Although there may very well be some unfairness associated with Colonial Pipeline's situation of having won appellate decisions holding that its pipelines are personal property and then having those victories taken away by legislature, the legislature, however, has broad taxing authority and the reclassification has a reasonable relationship to a legitimate state interest. Under the rational basis test, accordingly, the Court concludes that there is no equal protection violation attendant to the reclassification of Colonial's pipeline from personal property to real property.

Public Utility Classification

Colonial has market and eminent domain power. Its rates are subject to government regulation. Its pipelines cannot be used or rented by other companies. It has certain features of a natural monopoly even though the parties agree that it is not an actual monopoly. Although reasonable minds certainly disagree, the Court concludes there is a rational basis for classifying Colonial Pipeline and its property under the public utility classification.

Applying the equal protection standard, the Court finds that Defendants have demonstrated a rational basis to classify Colonial's pipeline as public utility property, and that Colonial has failed to meet its heavy burden of negating every conceivable basis to support this tax classification. As a general rule, public utilities include companies that provide "necessary services to the public, such as telephone lines and services, electricity,

and water,” most of which “operate as monopolies but are subject to governmental regulation.” Black’s Law Dictionary 1544 (7th ed. 1999). As our Supreme Court once explained, “by their very nature and because of the character of their operations, most public utilities are regulated monopolies. None enjoy continuing exclusivity and all are regulated in the public interest and enjoined to meet the public need.” *Nashville Mobilphone Co. v. Atkins*, 536 S.W.2d 335, 340 (Tenn. 1976).

In Tennessee, public utility companies and common carriers historically have enjoyed the right of eminent domain and have been subject to government rate regulation. See, e.g., *Chapdelaine v. State Bd. of Exam’rs for Land Surveyors*, 541 S.W.2d 786 (Tenn. 1976); *Nashville Water Co. v. Dunlap*, 138 S.W.2d 424 (Tenn. 1940); *Memphis News Publ’g Co. v. Southern Ry. Co.*, 75 S.W. 941 (Tenn. 1903); *West Tenn. Power & Light Co. v. Shallabarger*, 14 Tenn. App. 258 (1931); *Oman v. Tennessee Cent. Ry. Co.*, 7 Tenn. App. 141 (1927). Indeed, although not exclusive, the right of eminent domain and submission to rate-setting procedures have been recognized as “two distinguishing characteristics of public utilities.” Robyn L. Thiemann, *Property Devaluation Caused by Fear of Electromagnetic Fields: Using Damages to Encourage Utilities to Act Efficiently*, 71 N.Y.U. L. Rev. 1386, 1393 (1996).

In the present case, the undisputed evidence demonstrates that Colonial enjoys the right of eminent domain in Tennessee and is subject to rate regulation by the Federal Energy Regulatory Commission (FERC). Thus, Colonial possesses at least two of the distinguishing characteristics of public utilities in general and, in particular, public utilities in Tennessee. Additionally, Defendants’ expert proof established that Colonial has market power. The existence of these characteristics provides a reasonable basis for the General Assembly’s decision to classify Colonial’s pipelines as public utility

property. Colonial operates a continuous refined petroleum products pipeline that transports fuel to various delivery points in 13 states and the District of Columbia. Since the enactment of Tennessee's modern classification scheme in 1973, the property of pipeline companies has been classified and assessed as public utility property. *See* 1973 Tenn. Pub. Acts. 226, § 6. To this day, refined petroleum and natural gas pipelines continue to be assessed as public utilities, and Colonial did not present sufficient evidence that would overcome the presumption of constitutionality or demonstrate that a different classification of its property is required.

Contrary to Colonial's contention, Colonial is not similarly situated to the other taxpayers referenced in its Amended Complaint that also transport refined petroleum products. Like Colonial, railroads and barges have the ability to transport refined petroleum products over long distances. By volume, however, they ship only a fraction of the amount of refined petroleum products shipped by Colonial. For example, railroads ship less than 2 percent of the amount of refined petroleum products into Tennessee than is shipped in by Colonial. Barges arriving in Tennessee from locations where Colonial has a presence similarly ship a very small percentage of the volume shipped into Tennessee by Colonial.

In contrast, Colonial delivers about 20 percent of all refined petroleum products delivered by pipeline in the United States and 65 percent of all products delivered in the southeastern states. From this proof, it appears that Colonial enjoys a sizeable market share for the delivery of refined petroleum products in Tennessee and the United States. In fact, some authorities in the field cite oil pipelines as an example of a "natural monopoly," which is yet another characteristic of a public utility. *See, e.g.,* Dylan Cors, *Breaking the Bottleneck: The Future of Russia's Oil Pipelines*, 7 Duke J. Comp. & Int'l

L. 597, 599 (1997); Roger A. Boner, *Antitrust Policy in Ukraine*, 31 Geo. Wash. J. Int'l L. & Econ. 1, 37 (1997); Shelley R. Saxer, *Government Power Unleashed: Using Eminent Domain to Acquire a Public Utility or Other Ongoing Enterprise*, 38 Ind. L. Rev. 55, 60 (2005); David J. Teece, *Telecommunications in Transition: Unbundling, Reintegration, and Competition*, 1 Mich. Telecomm. & Tech. L. Rev. 47, 53 (1995).

Colonial has competition in the transportation of refined petroleum products. This competition is both direct (Plantation) and indirect (trucks, rail, barges). The Court concludes that Colonial does not compete with refineries, specifically the Valero refinery located in West Tennessee. Refineries convert natural sources, through a manufacturing process, into refined petroleum products that are placed into various distribution systems to carry the product to ultimate consumers. The Court notes, however, that there is a legitimate question raised by the differences in state and local tax treatment of these classifications for assessment purposes as highlighted in the proof at trial. It makes common sense for the challenged statutory classification to be followed in every municipality and government subdivision in Tennessee. The Court concludes that these differences mostly clearly relate to Colonial's as applied challenge. The statutory public utility classification, as written, is supported by a rational basis and does not constitute a facial violation of Colonial's right to equal protection.

Uniformity Clause

As amended in 1972, Article II, Section 28 of Tennessee Constitution provides, *inter alia*, that "[t]he ratio of assessment to value of property in each class or subclass shall be equal and uniform throughout the State, the value and definition of property in each class or subclass to be ascertained in such manner as the legislature shall direct." *Id.* Tennessee appellate courts have noted that this provision gives the Legislature "very

broad discretion” to determine the value and definition of property in each of the classifications or subclassifications contained in Article II, Section 28. *See In re All Assessments*, 58 S.W.3d 95, 99 (Tenn. 2000); *Sherwood Co. v. Clary*, 734 S.W.2d 318, 321 (Tenn. 1987); *Kellogg Co. v. Assessment Appeals Comm’n*, 978 S.W.2d 946, 951 (Tenn. Ct. Ap. 1998). As the Supreme Court opined when it discussed the 1972 amendment to Article II, Section 28, “the General Assembly was not constitutionally required to attempt to administer and maintain an impractical system of taxation, and it was given *very broad discretion* with respect to determining the value and definition of property in each of the authorized classifications or subclassifications.” *Sherwood Co.*, 734 S.W.2d at 321 (emphasis added).

Property tax classifications are subject to the “principles of uniform taxation” under Article II, Section 28 of the Tennessee Constitution (The “Uniformity Clause”). Tenn. Op. Att’y Gen. 03-068 (2003), 2003 WL 21362766, at *2. “The equality and uniformity requirement of Article II, Section 28 applies across the classes and subclasses created by the Constitution” – “that is, the equality and uniformity of taxation required, are equality and uniformity with taxes on property of like character[.]” *Mall of Memphis Assocs. v. Tennessee State Bd. of Equalization*, No. 106118-3, 1997 WL 436222, at **8,9 (Aug. 1, 1977) (internal quotation and citation omitted); *see also Louisville & Nashville R.R. Co. v. Public Serv. Comm’n*, 631 F.2d 426, 431 (6th Cir. 1980) (rejecting the Board’s contention that the Uniformity Clause “requires only that the ratio of assessment to value be equal and uniform within each class or subclass” and emphasizing that “the constitutional requirement that all property must be valued at full market value would be emasculated by the adoption of this contention”).

Even if a “reasonable basis exists” for classifying certain property “differently from other property” for equal protection purposes, that “is not sufficient to satisfy the uniform taxation clause, because under that clause any authorized methodology must seek to reach the true value of the property, regardless of” of any other technical differences. Tenn. Op. Att’y Gen. 03-068 (2003), 2003 WL 21362766, at *2. The question generally “require[s] a factual inquiry to determine whether the methodology” set forth in the statute “is so divorced from reality that it becomes unconstitutional.” *Id.* The Court concludes that this question of uniformity triggers a uniquely as applied inquiry that should be first addressed by the administrative agency in the as applied challenged hearing. As discussed above under the equal protection analysis, there is a facial rational basis for the classification at issue here when viewed in light of the state constitutional Uniform Taxation provision. Stated differently, there is no constitutional infirmity on the face of the real property utility classification under the Uniformity Clause of the Tennessee Constitution.

Commerce Clause

The constitutional proviso that Congress “shall have power . . . to regulate commerce . . . among the several states” necessarily prohibits states from adopting legislative measures that “regulate” interstate commerce. *See* U.S. Const. art. I, § 8, cl. 3. One of the fundamental values in Commerce Clause jurisprudence is that states cannot engage in economic protectionism at the expense of other states or interstate commerce. Commerce Clause precedent limits the extent to which states and localities may “regulate or otherwise burden the flow of interstate commerce.” *Maine v. Taylor*, 477 U.S. 131, 151 (1986). In this context, whether a measure is viewed as protectionist turns on “whether it can fairly be viewed as a law directed to legitimate local concerns, with

effects upon interstate commerce that are only incidental.” *Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978). On the other hand, our Constitution, including the Commerce Clause, features a basic framework (federalism) that posits that state and local governments retain certain zones of autonomy.

Recently, the Sixth Circuit reiterated its approach to Commerce Clause challenges:

This Circuit has adopted a two-step analysis to evaluate challenges to the dormant Commerce Clause. *Int’l Dairy Foods Ass’n v. Boggs*, 622 F.3d 628, 644 (6th Cir. 2010). Under the first step, we must determine whether “a state statute directly regulates or discriminates against interstate commerce, or [whether] its effect is to favor in-state economic interests over out-of-state interests.” *Id.* (quoting *Brown-Forman*, 476 U.S. at 579, 106 S. Ct. 2080). “A [state regulation] can discriminate against out-of-state interests in three different ways: (a) facially, (b) purposefully, or (c) in practical effect.” *Id.* at 648 (quoting *E. Ky. Res. v. Fiscal Court of Magoffin Cnty. Ky.*, 127 F.3d 532, 540 (6th Cir. 1997)). “[T]he critical consideration is the overall effect of the statute on both local and interstate activity.” *Brown-Forman*, 476 U.S. at 579, 106 S. Ct. 2080. The plaintiff bears the initial burden of proof to show that the state regulation is discriminatory. *Davis*, 553 U.S. at 338, 128 S. Ct. 1801.

If the plaintiff satisfied its burden, then “a discriminatory law is virtually *per se* invalid and will survive only if it advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives.” *Id.* at 328, 128 S. Ct. 1801 (quoting *Or. Waste Sys., Inc.*, 511 U.S. at 101, 114 S. Ct. 1345 (internal citation omitted)). However, if the state regulation is neither discriminatory nor extraterritorial, then the court must apply the balancing test established in *Pike*. Under the *Pike* balancing test, a state regulation is upheld “unless the burden it imposes upon interstate commerce is ‘clearly excessive in relation to the putative local benefits.’” *Int’l Dairy*, 622 F.3d at 644 (quoting *Pike*, 397 U.S. at 142, 90 S. Ct. 844).

American Beverage Ass’n v. Snyder, 700 F.3d 796, 803-04 (6th Cir. 2012). The United States Supreme Court has held that state taxes will be upheld against dormant Commerce Clause challenges if: 1) the tax was applied to an activity that had a “substantial nexus” with the taxing state; 2) the tax was “fairly apportioned;” 3) the tax did not “discriminate against interstate commerce;” and 4) the tax was “fairly related” to the services provided

by the taxing state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). Over the years, the Court has continued to apply this four-part test in evaluating challenges to state tax laws under the dormant Commerce Clause.

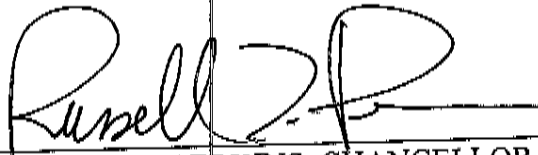
In a discrimination case under the Commerce Clause, the statutory measure itself is the starting point. In other words, the first thing to determine in a dormant Commerce Clause challenge is whether the measure, on its face, prescribes “differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.” *Oregon Waste Sys, Inc. v. Department of Envtl. Quality*, 511 U.S. 93, 99 (1994). If the “statute directly regulates or discriminates against interstate commerce, or when its effect is to favor in-state economic interests over out-of-state interests, [the courts] have generally struck down the statute without further inquiry.” *Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573, 579 (1986). Here, the challenged classification statutes do not contain language indicating a difference in treatment based on local versus interstate interests. For the same reasons mentioned under the equal protection discussion, trucks, barges, rail, and refineries, are not similarly situated with Colonial Pipeline for Commerce Clause purposes. *See DirecTV, Inc. v. Roberts*, 477 S.W.3d 293, 305-07 (Tenn. Ct. App. 2015). The Court, therefore, concludes that there is no facial Commerce Clause infirmity with the challenged (real property and public utility property) statutory classifications.

Conclusion

Based on the foregoing, the Court concludes that the statutory classifications of property provided for in Tenn. Code Ann. §§ 67-5-501(9)(B)(iii) & 67-5-501(8), and related statutory provisions challenged by Colonial Pipeline, are facially constitutional. The Court, therefore, DISMISSES Plaintiff’s Amended Complaint with prejudice. The

Court taxes Court costs, for which execution may issue, against Plaintiff, Colonial Pipeline Company.

IT IS SO ORDERED.



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